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SUBJECT: RUSSIAN BANKS ACTIVE IN UKRAINE

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¶1. (SBU) Summary. While other foreign-owned banks have shrunk their balance sheets, deep-pocketed Russian banks have expanded and increased their market share in Ukraine. VTB Bank (formerly Vneshtorgbank) and Vnesheconombank (VEB), two Russian state-owned banks, have made several high profile acquisitions in the last three years and are now among Ukraine's ten largest banks, along with privately owned Alfa Bank. Despite their aggressive expansion, Russian banks still only account for roughly 12% of total banking assets and are unlikely to significantly increase their position in the short- to medium-term. End Summary.

ACTIVE PLAYERS IN UKRAINE

¶2. (U) Ten of Ukraine's 185 banks are Russian-owned. The Russian banks range in size from some of the country's largest institutions to small lenders that barely meet regulatory capital requirements. Alfa Bank Ukraine, with \$4.24 billion in assets, is Ukraine's seventh largest bank. Prominvestbank, recently acquired by VEB, has \$3.85 billion in assets and is the country's eighth-largest bank. VTB Bank Ukraine, with \$3.53 in assets, is Ukraine's tenth-largest bank. Other mid-size Russian banks are privately held Delta Bank, Sberbank Ukraine (a subsidiary of Russia's behemoth state-owned bank), and BM Bank (a subsidiary of the Bank of Moscow).

ALFA BLAZES TRAIL

¶3. (U) Large Russian banks have expanded operations by acquiring domestic financial institutions. Alfa Bank Ukraine purchased Kievinvestbank in 2000, after it had established a local subsidiary to serve as a corporate treasury for the Alfa Group's assets in Ukraine, which include major interests in oil and gas (TNK-BP), telecommunications (Vimpelcom, Kyivstar), and media (CTC). With the acquisition, Alfa Bank has since expanded to offer a full range of retail and corporate banking services.

¶4. (SBU) An Alfa Bank executive acknowledged to us that the Group's connections with the Kremlin had benefitted their overall business interests, but that Alfa Bank's investment decisions in Ukraine had been seen through a pure business lens. He said the bank channels funds from some of its most profitable divisions like oil or telecommunications to its banking division in an effort to increase its market share.

¶5. (U) The Alfa Group, founded by Russian oligarchs Mikhail Fridman and Pyotr Aven, is one of Russia's largest privately owned financial and industrial conglomerates. Alfa Bank, the group's banking subsidiary, is Russia's largest private bank.

OTHER MAJOR RUSSIAN ACQUISITIONS

¶16. (U) Russian state-owned banking groups have followed similar strategies. VTB Bank (then Vneshtorgbank), VEB, and Sberbank established subsidiaries in Ukraine to serve large (often state-owned) Russian corporate customers. They later purchased local lenders to acquire necessary infrastructure for universal commercial banking operations.

¶17. (U) VTB Bank purchased a 98% stake in Kyiv-based Mriya Bank in 2006, then owned by Ukraine's current Foreign Minister Poroshenko. In early 2009, VEB (Russia's economic development bank), bought 98% of Prominvestbank, an embattled lender that had been in state receivership since October 2008. Sberbank acquired small Kyiv-based NRB in December 2007. CEO German Gref said then he planned to inject \$400 million in capital and expand the bank's assets so that Sberbank could become one of Ukraine's top-ten banks within three years.

GEOGRAPHY DRIVES EXPANSION

¶18. (U) Russia is Ukraine's largest trading partner and one of its largest investors. Moreover, Ukraine's relative lack of banking sector development, which had made the country attractive to foreign players including Austria's Raiffeisen, Italy's UniCredit, and France's BNP Paribas, remains an important draw for Russian banks looking for growth opportunities beyond Russian borders. Russia's biggest banking groups can often draw on resources unrelated to their core banking activities. State banks have the explicit backing of the Russian government, while private institutions, like Alfa Bank Ukraine, draw on sizable financial resources of parental institutions.

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"RUSSIFICATION" OF UKRAINIAN BANKING SECTOR UNLIKELY

¶19. (SBU) Despite high ambitions and deep pockets, Russian banks are unlikely to significantly change the landscape of Ukraine's well-diversified banking sector, local analysts say. Prominvestbank, the largest Russian-owned bank in Ukraine, is only about a third of the size of Privatbank, Ukraine's largest lender. Local subsidiaries of Raiffeisen, BNP, and Unicredit are also significantly bigger than their Russian counterparts. Moreover, some analysts remain skeptical about Russian banks' appetite to further expand, given the National Bank of Ukraine's non-transparent refinancing decisions and numerous restrictions seemingly targeting foreign-owned banks.

COMMENT

¶10. (SBU) Given the close economic ties between the two countries, Russian banks' increased activity in Ukraine is hardly surprising. Moreover, Russian banks, which often rely on the state or their parental business structures for funding, are among the few players with the capital to expand their operations, either organically or through acquisitions. Yet, according to analysts, while their recent forays into Ukraine have come at a time when most other foreign players are downsizing their operations, they are unlikely to significantly tip the scales in the country's diversified banking sector.